

## Message Text

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TAGS: ETRD, GATT,IS

SUBJECT: GATT BOP CONSULTATION WITH ISRAEL

REF: GENEVA 8107

1. U.S. DEL TO GATT BOP CONSULTATIONS WITH ISRAEL ON MAY  
29 SHOULD BE GUIDED BY THE FOLLOWING INSTRUCTIONS.

2. U.S. DEL SHOULD MAKE FOLLOWING POINTS:

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A. THE UNITED STATES NOTES THE NOTABLE IMPROVEMENT IN  
ISRAEL'S BALANCE OF PAYMENTS AND WELCOMES THE SUBSTANTIAL  
LIBERALIZATION IN ISRAEL'S TRADE POLICY WHICH WAS INSTITU-  
TED LATE IN 1977.

B. IN VIEW OF THIS IMPRESSIVE PERFORMANCE AND ISRAEL'S

FAVORABLE BALANCE-OF-PAYMENTS PROSPECTS, THE UNITED STATES RECOMMENDS THE EARLY ELIMINATION OF ISRAEL'S REMAINING LICENSING RESTRICTIONS.

3. USDEL MAY POSE THE FOLLOWING QUESTIONS, AS APPROPRIATE:

A. DOES THE ISRAELI REPRESENTATIVE EXPECT THE GOVERNMENT BUDGET TO CONTINUE IN SUBSTANTIAL DEFICIT IN 1978?

B. IF INFLATION WERE TO CONTINUE AT A 40-45 PERCENT RATE IN THE NEXT THREE-FOUR MONTHS, WILL THE GOVERNMENT CONSIDER ADDITIONAL FISCAL AND MONETARY MEASURES TO RESTRAIN INFLATION?

C. WHAT EFFECT DOES THE ISRAELI GOVERNMENT EXPECT THE 1977 LIBERALIZATION MEASURES TO HAVE ON IMPORTS? ON THE CURRENT ACCOUNT?

D. TO WHAT DOES ISRAEL ATTRIBUTE THE STRONG PERFORMANCE OF THE CAPITAL ACCOUNT IN 1976 AND 1977? DO THE GOVERNMENT'S LATEST FIGURES FORESHADOW A STRONG PERFORMANCE IN 1978?

E. WHAT IS THE TOTAL TRADE COVERAGE OF THE ITEMS STILL SUBJECT TO IMPORT LICENSING, BOTH AS AN ABSOLUTE AMOUNT LIMITED OFFICIAL USE

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AND AS A PERCENTAGE OF TOTAL IMPORTS?

F. WHAT PLANS DOES THE ISRAELI GOVERNMENT HAVE FOR REMOVAL OF ITS REMAINING LICENSING REQUIREMENTS.

4. DISCUSSION:

A. THE OIL PRICE INCREASE, AS WELL AS INCREASING DEFENSE EXPENDITURES, HAVE IMPOSED HEAVY ADJUSTMENT BURDENS ON THE ISRAELI ECONOMY IN THE LAST FOUR YEARS. IN ORDER TO COPE WITH THESE BURDENS AND HOLD DOWN A SPIRALING INFLATION RATE, THE GOVERNMENT ATTEMPTED TO ADOPT CONTRACTIONARY MONETARY POLICIES IN 1974-1976 AND REDUCED ITS BUDGETARY DEFICIT. HOWEVER THE GOVERNMENT BUDGET CONTINUES TO RUN A LARGE DEFICIT BECAUSE OF DEFENSE EXPENDITURES AND DEBT SERVICING. WHILE THE EXTERNAL BALANCE HAS IMPROVED MARKEDLY, THE EFFECT ON THE DOMESTIC ECONOMY WAS SEVERE: GROWTH IN REAL GNP, WHICH HAD AVERAGED 8.5 PERCENT IN THE FIVE YEARS TO 1974, SLOWED TO 2.1 PERCENT, 0.9 PERCENT, AND 0.5 PERCENT IN 1975, 1976, AND 1977, RESPECTIVELY. SINCE THESE RATES WERE BELOW THAT OF POPULATION GROWTH, PER CAPITA INCOME ALSO DECLINED IN THOSE YEARS. THE AUTHORI-

TIES NOW EXPECT GNP TO GROW BY 4 PERCENT IN 1978 WITH AN IMPROVED TRADE PERFORMANCE AND A STRENGTHENING OF CONSUMPTION.

B. RATES OF INFLATION OF CONSUMER PRICES HAVE BEEN PERSISTENTLY HIGH, AT 39 PERCENT IN 1975, 31 PERCENT IN 1976, AND 42 PERCENT IN 1977. AMONG THE CAUSES WERE THE

REDUCTION OR PHASED ELIMINATION OF SUBSIDIES ON BASIC COMMODITIES, AN INCREASE IN PUBLIC UTILITY CHARGES, THE INTRODUCTION OF A VALUE ADDED TAX IN JULY 1976, AND THE POLICY OF SMALL, FREQUENT DEVALUATIONS OF THE ISRAELI POUND. ADDITIONAL PRESSURE WAS PROVIDED BY LARGE WAGE INCREASES IN 1976 AND 1977 (AVERAGE NOMINAL WAGES WERE LIMITED OFFICIAL USE

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48 PERCENT HIGHER IN 1977 THAN A YEAR EARLIER), BY WAGE INDEXATION, AND BY LARGE INCREASES IN CREDIT (87 PERCENT OVER 1976) AND MONEY SUPPLY (82 PERCENT OVER 1976) AS A CONSEQUENCE OF THE GOVERNMENT BUDGET DEFICIT. THE GOVERNMENT HAS SAID THAT THE INFLATION RATE WILL BE ONLY 30 PERCENT IN 1978, BUT DATA FOR THE FIRST FIVE MONTHS SUGGEST A MUCH HIGHER RATE, PERHAPS MATCHING LAST YEAR'S 42 PERCENT. IN MAY ALONE PRICES ROSE 5.5 PERCENT.

C. THE DEFICIT ON GOODS AND SERVICES, AS WELL AS THE CURRENT ACCOUNT DEFICIT, FELL DRAMATICALLY FROM 1975 TO 1977. THE CURRENT ACCOUNT DEFICIT FELL FROM MORE THAN \$2 BILLION IN 1975 TO SOMETHING OVER \$500 MILLION IN 1977, DUE TO HIGHER EXPORT RECEIPTS AND A SWING IN NET SERVICES FROM DEFICIT TO SURPLUS. IN 1976 AND 1977, LONG-TERM CAPITAL INFLOWS MORE THAN MADE UP THE DEFICIT, PRODUCING SURPLUS IN THE OVERALL BALANCE AND INCREASES IN OFFICIAL RESERVES. SEE IMF DOC. SM/78/111 AND EB/CGATT/78/2 FOR FURTHER DETAILS.

D. ISRAEL'S POLICY OF FREQUENT SMALL DEVALUATIONS OF THE POUND, REPLACED BY A FLOATING EXCHANGE RATE IN OCTOBER 1977, WAS IN LARGE PART RESPONSIBLE FOR THE IMPROVED EXPORT PERFORMANCE. IN 1978, THE TRADE BALANCE SHOULD SHOW A SLIGHT IMPROVEMENT DESPITE INCREASED IMPORTS. MOREOVER, FURTHER IMPROVEMENT IN THE SERVICES ACCOUNT IS EXPECTED, AND A CONTINUED STRONG CAPITAL ACCOUNT SHOULD PERMIT THE OVERALL BALANCE TO REGISTER A LARGER SURPLUS THAN IN 1977. LATE IN 1977, A MAJOR PACKAGE OF TRADE-LIBERALIZING ACTIONS WAS IMPLEMENTED.

D. BOP/187 DESCRIBES THE SUBSTANTIAL LIBERALIZATION OF THE ISRAELI IMPORT REGIME INTRODUCED AS PART OF THE NEP. LIMITED OFFICIAL USE

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THE CIRCA 300 ITEMS STILL SUBJECT TO LICENSING HAVE BEEN ESTIMATED TO COVER ONLY 10-15 PERCENT OF ISRAELI IMPORTS. THE IMF BELIEVES THAT THESE RESTRICTIONS ARE OF MINOR SIGNIFICANCE AS BALANCE-OF-PAYMENTS MEASURES, BUT THE ISRAELIS CLAIM THAT THE NEP HAS ONLY BEEN IN EFFECT FOR A FEW MONTHS AND THE BOP SITUATION IS STILL TENUOUS. UNDER THESE CIRCUMSTANCES, THE U.S. REPRESENTATIVE SHOULD WORK TOWARD A COMMITTEE RECOMMENDATION FOR THE EARLY ELIMINATION OF THE REMAINING RESTRICTIONS RATHER THAN A FINDING THAT ISRAELI IS NO LONGER APPLYING RESTRICTIONS FOR BOP PURPOSES. VANCE

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